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SUBJECT: BRAZIL - FOLLOW UP ON AMB. SOBEL'S MEETING WITH DEPUTY USTR
VERONEAU

REF: 06 STATE 193863

This cable is sensitive but unclassified, please protect accordingly.

¶1. (SBU) Summary: Post appreciates USTR's thoughtful and considered outline (reftel) of potential initiatives that the USG might pursue bilaterally with Brazil to enhance the trade relationship. After reviewing those ideas put forth, we believe the area of greatest near term potential is a bilateral steel forum. Although sensitivities on both sides may initially limit the scope of topics discussed in such an initiative, mutual confidence built over time may allow for additional subjects to be broached as well. Post also supports the idea of asking Brazil to lower tariffs on certain integrated circuits as well. Unfortunately, Brazil has placed on hold Congressional ratification of bilateral investment treaties with many countries due to differences over whether it can constitutionally submit government agencies to binding foreign arbitration. End Summary.

Steel Forum

¶2. (SBU) Brazil is a major steel producer and exporter, which, like the steel industry United States, views with some concern China's emergence as a new steel competitor. Brazil has long-standing and extensive supply links with U.S. industry, from pig iron that feeds many U.S. steel mills, to unfinished steels that are further processed by U.S. mills. Moreover, given acquisitions and mergers, the Brazilian steel industry has a growing stake directly in the U.S. steel industry. These commonalities form a promising ground for a bilateral forum.

¶3. (SBU) We would expect that at least initially there would be some subjects that the Brazilians would not want broached, or the raising of which would make them view USG intentions for the forum with suspicion. Foremost among these are recent allegations of slave labor conditions in the Brazilian charcoal industry, which provides inputs to local pig iron producers and through them ultimately to U.S. industry. The GoB is cooperating with a DHS/ICE investigation into labor conditions at these charcoal camps but we expect that it would want to keep the affair in law enforcement channels.

¶4. (SBU) National Development Bank (BNDES) support for Brazil's steel industry likely would be another sensitive point for the Brazilians. For the GoB, overall BNDES support for industry, including steel, is not negotiable. The GoB is unlikely to see much purpose in a bilateral dialogue with the USG on the point (although they may be willing to clarify specific questions on the mechanics

of BNDES financing). Brazil nevertheless has negotiated constraints and limits on BNDES financing. For example, Brazil engaged constructively in the recent successful negotiation, under OECD auspices, of the aircraft finance understanding. Brazil's goals in that process were two-fold: a) to limit the costs of export finance to the national treasury; and, 2) to ensure fairer competition and clear rules of the game with Canada, Brazil's main rival in that sector. It is possible that Brazil's concern with China's emergence as a competitor in steel would create an opportunity for engagement.

Whether that concern would be sufficient to overcome Itamaraty's south-south cooperation focus on China and join a WTO subsidies case is an open question.

Integrated Circuits

15. (SBU) Post also supports the idea of asking Brazil to join the WTO Information Technology Agreement, or alternatively, the Government/Authorities Meeting on Semiconductors (GAMS) in reducing to zero the duties on Multi Chip Packages (MCPS). The GoB desires to support development of a larger semi-conductor industry in Brazil to feed its existing electronics industry, but these plans would not necessarily conflict with the tariff reductions on MCPS.

SOBEL